

The enterprise zone building materials exemption allows retailers located in the municipality or unincorporated area of a county that established an enterprise zone to make tax-free sales of building materials that will be incorporated into real estate located in the enterprise zone. See 86 Ill. Adm. Code 130.1951. (This is a PLR).

July 7, 2000

Dear Xxxxx:

This Private Letter Ruling, issued pursuant to 2 Ill. Adm. Code 1200 (see enclosed), is in response to your letter of December 6, 1999. Review of your request for a Private Letter Ruling and your addendum disclosed that all information described in paragraphs 1 through 8 of subsection (b) of the enclosed copy of Section 1200.110 appears to be contained in your request. This Private Letter Ruling will bind the Department only with respect to COMPANY for the issue or issues presented in this ruling. Issuance of this ruling is conditioned upon the understanding that neither COMPANY nor a related taxpayer is currently under audit or involved in litigation concerning the issues that are the subject of this ruling request.

In your letter, you have stated and made inquiry as follows:

On behalf of our client, COMPANY we respectfully request the Illinois Department of Revenue to issue a private letter ruling pursuant to 2 Ill. Adm. Code Section 1200.110 with respect to the following factual situation.

General Information

- 1) Enclosed please find an original Form IL-2848, Power of Attorney, authorizing BUSINESS to represent COMPANY (the 'Company') before the Illinois Department of Revenue ('Department').
- 2) This Private Letter Ruling ('PLR') is not requested with regard to hypothetical or alternative proposed transactions. The PLR is requested to determine the Retailer's Occupation Tax consequences of the actual business practices of the Company.
- 3) The Company is not currently engaged in litigation with the Department in regard to this or any other tax matter.
- 4) The Department has not previously ruled regarding this matter for the Company. Neither the Company nor BUSINESS has submitted the same or similar issue to the Department.
- 5) The Company requests that certain information be deleted from the PLR prior to dissemination to others. The Company requests that its name, address, location of its facility, the description of the facility (including reference to # megawatt) and the name of its representative be deleted.
- 6) The Company knows of no authority contrary to the authorities referred to and cited below.

Statement of Material Fact

- 1) The Company is in the business of owning and operating electric generating facilities.
- 2) The Company is constructing a nominal # megawatt natural gas fired power plant (hereafter referred to as the 'Facility') in unincorporated CITY, Illinois.
- 3) The construction of the Facility will begin in May 2000.
- 4) It is anticipated that the Facility will be located within the COUNTY Enterprise Zone.
- 5) The Company will purchase significant materials from a retailer located in the enterprise zone, as provided in 86 Ill. Admin. Code Section 130.1951, for the purpose of qualifying for the 'enterprise zone building materials exemption.'
- 6) The following items represent the significant materials that will be purchased from a retailer within the enterprise zone for incorporation into the Facility. Please refer to the attached summary describing these items and the manner in which they are affixed to the realty. These materials will be referred to herein after as 'the materials.':
 - a) Concrete foundations for building and equipment support.
 - b) Eight (8) natural gas fired turbine generators.
 - c) Electrical equipment including, four (4) main transformers and above-ground and below-ground electrical conduit and cabling.
 - d) Piping for water and natural gas supply and wastewater discharge.

Ruling Requested

The major materials identified in the attachment qualify as 'building materials' for the purpose of the Retailer's Occupation Tax deduction provided in 35 ILCS 120/5k and 86 Ill. Admin. Code Sec. 130.1951(1).

Relevant Authorities

The Illinois Retailers' Occupation Tax Act [35 ILCS 120/2] imposes a tax on persons engaged in the business of making retail sales of tangible personal property. In accordance with Section 2-10 of the Act, this tax is measured by a seller's gross receipts [35 ILCS 120/2-10]. Pursuant to Section 5k of the Act [35 ILCS 120/5k], a retailer whose place of business is located within a county or municipality which has established an enterprise zone, and who makes sales of 'building materials' to be incorporated into real estate in that enterprise zone by remodeling, rehabilitation or new construction, may deduct receipts from such sales in the calculation of taxable gross receipts.

For purposes of our analysis, we have assumed that the Company will purchase all qualifying building materials from a retailer located within COUNTY.

Therefore, our analysis focuses on the requirement that, in order to qualify for the deduction, the materials must constitute 'building materials' as provided in 86 Ill. Adm. Code Sec. 130.1951(a)(7). The regulation also states that to qualify as a 'building material,' the item must be for 'physical incorporation into real estate.'

Therefore, the question is whether the items at issue would qualify as 'building materials,' that is, whether the items are purchased for 'physical incorporation into real estate.' In Commonwealth Edison v. Property Tax Appeal Board, 219 Ill. App. 3d 550 (2d Dist. 1991), the Illinois Appellate court ruled that an electric utility's power generating machinery and equipment, including turbine generators, were properly classified and assessed as real property, and not personalty.

The court's decision was based on prior decisions in Cherry Bowl, v. Property Tax Appeal Board, 100 Ill.App.3d 326 (1981); Ayrshire Coal v. Property Tax Appeal Board, 19 Ill.App.3d 41 (1974); and In re Application of Beeler, 106 Ill.App.3d 667 (1982). Citing these decisions, the appellate court found that under the 'intention test,' three criteria must be evaluated to decide whether an item of tangible personal property becomes a fixture to realty. First, the property must be annexed to the realty or to something appurtenant thereto; second, the property must be applied to the use or the purpose to which that part of the realty with which it is connected is appropriated; and third, the party making the annexation must intend to make a permanent accession to the freehold.

Applying the 'intention test,' the court found that the machinery and equipment was sufficiently affixed to the real estate; the machinery and equipment were applied for the use and the purpose to which the power plant was devoted; and the utility intended the machinery and equipment to be a permanent accession to the property. Therefore, the court determined the machinery and equipment was properly classified as real property.

It appears that the Department follows the 'intention test' as set forth in *Commonwealth Edison* for Retailer's Occupation Tax purposes. In ST-88-0961 (December 22, 1988), the Department, in referring to the decision in In re Application of Beeler, stated that in order to be physically incorporated into real estate, an item must be applied to the use or purpose to which that part of the realty which it is connected is appropriated, and the party making the annexation must intend to permanently improve the real estate.

In a more recent decision, the Department in Private Letter Ruling ST-99-0009 (March 9, 1999) ruled that pipe racks, pipe, supports, and piping tie-ins installed at a natural gas fired power plant would constitute 'building materials' under the Department's regulations because they were permanently affixed to real estate. Further, since the real estate was located within an enterprise zone such items incorporated into real estate could be purchased tax-free from qualified retailers.

Pursuant to the above cited regulations, cases, and PLRs, the 'intention test' is to be applied in answering the question of whether an item qualifies as a 'building material' for purposes of the deduction at issue here. The facts indicate that under the intention test, the materials qualify as building materials and consequently the receipts from the sale of the materials are deductible under 35 ILCS 120/5K and 86 Ill. Adm. Code Sec. 130.1951(1).

First, the significant items at issue here will be permanently affixed to the realty. Please refer to the attached schedule for details on the method of affixation. Second, the items will be applied for the use and purpose to which the realty is dedicated, i.e., the generation of electricity. The real property as a whole is dedicated and zoned for the purpose of operating an electric generating station. The materials in question comprise the major components of the facility. Third, the accession of the items is intended to remain permanent. The Company's management has indicated they have no intention to, at any time, sell or dispose of any of the materials other than as part of the sale of the facility. The Company's management has further indicated that if the materials or real property were ever to be sold, they would be sold together as a sale of an 'electric generating station' and that they would not consider selling or disposing of any components thereof.

To remove any of the major materials, including the gas turbine generators, would result in substantial damage to the materials and realty. The anchor bolts which are embedded in the concrete foundation would have to be removed. Removing the anchor bolts would will result in damage to the anchor bolts, foundation, underground electrical cable and piping, and possibly damage the gas turbine generator. Therefore, this demonstrates that the equipment, after being attached, would be permanently affixed.

Conclusion

The deduction provided in 35 ILCS 120/5k is applicable to receipts from the sales of 'building materials.' In order to qualify as 'building materials,' the items must be physically incorporated into real estate. In determining whether an item is physically incorporated into real estate, the Department uses the 'intention test' as outlined in *Commonwealth Edison*.

Applying the 'intention test' to the materials in question demonstrates that these items qualify as 'building materials' for purposes of the deduction provided in 35 ILCS 120/5k. First, the items will be annexed to the realty; second, the items annexed to the realty will be applied to the purpose to which the realty is dedicated (i.e., the generation of electricity); and third, the Company intends that the annexation remain permanent. Since the materials qualify as building materials incorporated into real estate in an enterprise zone, the materials may be purchased from a retailer in the zone free from Retailer's Occupation Tax and Use Tax.

We respectfully request that the Department issue a ruling stating that the materials described in the attachments qualify as 'building materials' for the purposes of the deduction provided in 35 ILCS 120/5k. If the Department can not conclude that the materials qualify as 'building materials', I request the Department contact me at ##### to determine what additional information is required or allow the taxpayer to rescind this ruling request.

Enclosed is a copy of 86 Ill. Adm. Code 130.1951 concerning Enterprise Zones. The enterprise zone building materials exemption allows retailers located in the municipality or unincorporated area of a county that established an enterprise zone to make tax-free sales of building materials that will be incorporated into real estate located in the enterprise zone. Section 130.1951(a) states, in part, as follows:

- 7) In order to qualify for the deduction, the materials being purchased must be building materials. That is, they must be purchased for physical incorporation into real estate. For example, gross receipts from sales of:
 - A) common building materials such as lumber, bricks, cement, windows, doors, insulation, roofing materials and sheet metal can qualify for the deduction;
 - B) plumbing systems and components thereof such as bathtubs, lavatories, sinks, faucets, garbage disposals, water pumps, water heaters, water softeners and water pipes can qualify for the deduction;
 - C) heating systems and components thereof such as furnaces, ductwork, vents, stokers, boilers, heating pipes and radiators can qualify for the deduction;

- D) electrical systems and components thereof such as wiring, outlets and light fixtures which are physically incorporated into the real estate can qualify for the deduction;
- E) central air conditioning systems, ventilation systems and components thereof which are physically incorporated into the real estate can qualify for the deduction;
- F) built-in cabinets and other woodwork which are physically incorporated into the real estate can qualify for the deduction;
- G) built-in appliances such as refrigerators, stoves, ovens and trash compactors which are physically incorporated into the real estate can qualify for the deduction;
- H) floor coverings such as tile, linoleum and carpeting that are glued or otherwise permanently affixed to the real estate by use of tacks, staples, or wood stripping filled with nails that protrude upward (sometimes referred to as "tacking strips" or "tack-down strips") can qualify for the deduction.

You assert in your letter that the materials are being purchased from a retailer located in the jurisdiction that created the enterprise zone into which the building materials will be incorporated. You have cited a list of cases which reflect decisions regarding the proper classification of property for property tax determinations. The manner in which property is classified for property tax is not conclusive in determinations of the enterprise zone building materials exemption under the Retailers' Occupation Tax.

Concrete and rebar, used in a foundation, qualify as building materials. Anchor bolts, electrical conduit and piping that will be embedded in the foundation qualify as building materials. The eight natural gas fired turbines that are constructed on-site and permanently affixed to the foundation with anchor bolts and hardwired to underground and aboveground electrical cabling and piping for natural gas and water supply qualify as building materials. The generator that is constructed on-site and permanently affixed to the foundation with anchor bolts and connected to underground and electrical cabling qualifies as a building material. The stack, which is attached to the concrete foundation with anchor bolts and welded together, qualifies as a building material. The inlet fogging system attached to the generator foundation with anchor bolts and hardwired into underground and aboveground cabling and piping for water supply, also qualifies as a building material. The accessory base, which is bolted to the foundation and connected to the turbine, qualifies as a building material.

In regards to the electrical equipment, the transformers that are attached with anchor bolts to a concrete foundation qualify as building materials. The underground cabling that is housed in conduit and encased in a concrete housing and is run 4 to 10 feet below the ground, does qualify as a building material. The aboveground cable that is physically attached to the foundation or equipment supports, which are attached to the foundation by anchor bolts, also qualifies as a building material.

The piping that is installed 4 to 10 feet below the ground and is encased in concrete qualifies as a building material. The aboveground piping supported by "T" supports that are attached to the foundation by anchor bolts or welded to equipment supports qualifies as a building material.

The facts upon which this ruling are based are subject to review by the Department during the course of any audit, investigation, or hearing and this ruling shall bind the Department only if the material facts as recited

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in this ruling are correct and complete. This ruling will cease to bind the Department if there is a pertinent change in statutory law, case law, rules, or in the material facts recited in this ruling.

I hope this information is helpful. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.